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Sup. Ct.

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1945

No. [redacted] 107

B. C. D. BYNUM, INDIVIDUALLY, AND B. C. D. BYNUM AND EARL COBB, AS INDEPENDENT EXECUTORS AND TRUSTEES UNDER THE LAST WILL AND TESTAMENT OF MARIE BYNUM SMITH, DECEASED,

Petitioners,

vs.

PHILLIPS PETROLEUM COMPANY

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS, FIFTH CIRCUIT.

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Of Counsel.

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SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1945

No. 1236

B. C. D. BYNUM, INDIVIDUALLY, AND B. C. D. BYNUM AND EARL COBB, AS INDEPENDENT EXECUTORS AND TRUSTEES UNDER THE LAST WILL AND TESTAMENT OF MARIE BYNUM SMITH, DECEASED,

Petitioners

vs.

PHILLIPS PETROLEUM COMPANY

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS, FIFTH CIRCUIT.

To the Honorable Chief Justice and the Associate Justices of the Supreme Court of the United States:

Petitioners B. C. D. Bynum, individually, and B. C. D. Bynum and Earl Cobb, as Independent Executors and Trustees under the last will and testament of Marie Bynum Smith, deceased, plaintiffs in the lower court and appellees in the Circuit Court of Appeals, respectfully pray that writ of certiorari issue to review a judgment of the United States Circuit Court of Appeals for the Fifth Circuit in Cause No. 11,239 on the docket of that Court. As reflected in the

opinion of that Court, it felt that the result, while justified by its interpretation of the law, was not a righteous judgment.

I

Opinions of the Circuit Court of Appeals

The opinions of the Circuit Court of Appeals have not yet been reported. The opinion of the majority of the Court on original hearing is shown at pages 535-542 of the record, and the opinion on rehearing at pages 556-557. The dissenting opinion is at pages 543-546.

II

Jurisdiction

Review is sought here under United States Code, Title 28, Sec. 347 (Judicial Code, Sec. 240). The judgment of the Circuit Court of Appeals was entered on February 1, 1946 (R. 543). Motion for Rehearing, filed on February 22, 1946 (R. 545), was denied March 11, 1946 (R. 558). This Petition for Certiorari is filed within 90 days thereafter.

III

The Questions Presented

The following questions are presented:

(1) Whether, because of the Texas law to the effect that an oil and gas lease reserving royalty of one-eighth the market price of gas reserves no interest in the gas itself, but provides only the obligation of lessee to pay the value thereof, a Federal Court is deprived of power to require lessee to make a full disclosure to lessor of all facts with respect to such gas and to fully and faithfully account to his lessor.

(2) Whether the provision in a gas lease for payment of "market price at the well" means market price at the wells drilled on the lease or, as the Court held, "the price which similar gas brings at the mouths of wells generally in the field."

(3) Whether a *prima facie* case of absence of market price cannot be made without showing the facts as to all wells "in the field" (in this case a field 125 miles in length, covering portions of 7 counties, and containing more than one and one-half million acres of land).

(4) Whether, under a lease providing for payment of royalty from gas at the rate of the "market price at the well", lessor can show the fair value of the gas at that point, after showing there are no competitive purchasers of gas in the County, and no pipeline or other outlet in the County purchasing the same kind of gas except defendant, and that all of its purchases are under long time contracts providing for advancement of well drilling costs and minimum purchases.

(5) Whether, for a "market price" to exist for gas from a particular well, there must be competitive purchasers for the gas from that well under such circumstances as that seller will obtain the benefit and incur the risks of fluctuations in the market; and whether such market must exist either at the well itself, or at some point to which the gas can be transported by existing facilities.

(6) Whether a *prima facie* showing as to absence of market price was made, sufficient to require lessee to go forward with the evidence, by showing:

> (a) That of the 243 sweet gas wells in the County there was not a single well whose production was sold under competitive conditions or under circumstances reflecting a market price at the well.

(b) That there was no outlet available to the gas produced except to lessee itself for its own operations.

(c) That lessee took only 8.57% of the allowable production from the well in 1943, and 35.11% in 1942, and offered no explanation as to the reasons for its failure to take the entire allowable production and sell that portion for which it had no use to some other purchaser, if there was one, offering a market for such gas.

(d) That lessee had never purported to make tenders of royalty on the basis of "market price" but had sent plaintiffs statements purporting to show "gasoline content and residue value", and made no explanation as to how those values were determined.

(7) Whether, as circumstances to be considered by the jury in determining the fair value of gas as distinguished from "market price", plaintiffs may show the prices on royalty gas being paid by various gas producers in the county to their royalty owners, and the prices paid by pipeline companies to producers under long term contracts.

(8) Whether the rights of defendant were fully protected by the trial court's instruction that factors of remoteness or differences in circumstances attending the prices considered must be given appropriate consideration.

IV

Summary Statement of Matters Involved

Petitioners, as lessors, sued respondent, as lessee, to recover royalties payable to them under two oil and gas leases which provided that the royalties payable should be as follows:

"• • • (b) on gas produced from said land and sold or used off the land or in the manufacture of gasoline, including casinghead gas, *the market price at the well* of one-eighth of the gas so sold or used,

provided that if and when lessee shall sell the gas at the wells lessor's royalty shall be one-eighth of the amount realized from such sale" (R. 71, 77).

There was no controversy as to the volumes of gas produced. Plaintiffs 2/3ds royalty interest was the equivalent of 311,524 MCF (R. 461). Respondent had tendered plaintiffs the equivalent of .788 of 1¢ per MCF (R. 462), aggregating $2,457.38. None of the tendered checks was accepted. The jury found that the fair value of the gas was 4¢ per MCF (R. 27), aggregating $12,460.96, more than four times the sums tendered by defendant. Defendant offered no testimony explanatory of the amounts of its checks.

Plaintiffs expressly pleaded that during the entire period involved there had been no market for the gas at the well, and, therefore, that the standard for royalty payments set out in the leases could not be applied; but that since Phillips had taken the gas and disposed of same or caused same to be used off the premises, it was obligated to pay for their royalty interest the fair and reasonable value at the well, which they alleged had been 4½¢ per MCF (R. 6-7).

The jury was informed by the court's charge that if there had been established in the field a market price, then plaintiffs were entitled to be paid one-eighth of that price; but, if not, that plaintiffs were entitled to be paid the fair and reasonable value of their royalty interest (R. 499-500). It was told that it should first determine whether a daily market price existed at the well for such gas, and, second, if there had been no such market price, then to determine what the gas was actually worth (R. 500).[1] The jury found that the *fair value* had been 4¢ per MCF (R. 27).

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[1] This charge was in almost the exact language as that used by the same Circuit Court of Appeals in *Sartor* v. *United Gas Public Service Co.*, 84 F. (2d) 436, 440. That language was expressly approved by this Court in *Sartor* v. *Arkansas Nat. Gas Corp.*, 321 U. S. 620, 622.

Evidence Admitted on Primary Issues.

(1) Plaintiffs in the District Court expressly pleaded that during the period of production there had been no market or market price at the well for their royalty gas (R. 6, Sec. XIII). In support of that allegation, they showed:

(a) that there were, in 1942, 231 wells, and, in 1943, 243 wells (R. 475) in the county producing the same kind of gas as that produced from the Bynum well;

(b) that, of those wells, 187 wells in 1942 and 188 in 1943 belonged to certain long distance pipeline companies, Canadian River Gas Company, Red River Gas Company, Texoma Natural Gas Company and Panhandle Eastern Pipe Line Company (R. 475), none of which sold gas at the wells, but all of which used the production from their wells in their own operations;

(c) that Phillips owned 11 wells in 1942 and 20 in 1943 (R. 473) selling no gas at the wells, but using all the production in its own operations;

(d) that Shamrock Oil and Gas owned three wells (R. 474), but sold no gas at the wells, using its production in its own operations;

(e) that Southwestern Public Service owned one well (R. 474), but sold no gas at the well, but used all the production in its own operations;

(f) that the production from three wells, two owned by Pan Oil Company and one by Northern Natural Gas Company (R. 472) was sold at or near the wells, but on long term written contracts made in 1935 (R. 359) or 1940 (R. 380);

(g) that Shamrock Oil and Gas Company owned 25 wells (R. 471), the production from which was, in 1937 sold to Panhandle Eastern for the life of the leases (R. 363);

(h) that Kerlyn Oil Company owned two wells, and Dave Rubin one well (R. 474), the production from which was in 1937 contracted to Phillips for the life of the leases under a complicated processing contract, involving provisions for minimum production, advancement of drilling costs, and other considerations (R. 527);

(i) that the only pipelines taking gas out of Moore County except those of Texoma, Canadian River and the Red River Company, none of which purchased gas, Panhandle Eastern, which was making no additional connections, were the Skelly line, which transported only sour gas, the Southwestern Public Service Company, which transported a small volume of gas from one well, and the Phillips line, which transported sweet gas that had been commingled with sour gas (R. 464);

(j) that the *only* gasoline plant in Moore County except those of defendant had never purchased sweet gas (R. 405); and;

(k) that Phillips' reports to plaintiffs had been based, not on "market price," but on "Sellers' Gasoline Content and Residue Value" (R. 89).

(2) As being appropriate for consideration in determining fair value of the gas, plaintiffs showed the prices being paid other royalty owners by producers in the county, other than Phillips, under leases and division orders fixing the price, and the prices being paid under long term purchase contracts by one of the pipeline companies.[2]

[2] In showing these prices, the wells were dealt with individually, so in the interest of brevity details as to such evidence are not deemed necessary here.

Holdings of the Majority of the Court

On appeal the Circuit Court of Appeals for the Fifth Circuit, by a divided court, reversed and remanded the case. The holdings of the majority are reflected in the Court's Original Opinion (R. 535) and its Opinion on Rehearing (556). In those opinions the Court held

(1) That, because of the Texas law that the royalty owner has no "title" to the ⅛th part of the gas, the Court was "unable to fasten the obligation to make a full disclosure where it really ought to be", on lessee to keep his lessor fully informed and to disclose all facts coming to his knowledge and to fully and faithfully account to his lessor (Original Opinion, R. 540).

(2) That the term "market price at the well" did not mean market price at the Bynum well but meant the "price which similar gas brings at the mouth of wells generally in the field" (Opinion on Rehearing, R. 557).

(3) That the *Sartor* cases, supra, were distinguishable from this case since in those cases it was a "matter of common knowledge that in the Richland Field such gas was *readily marketable* to pipeline companies", whereas, in the present case, it was conceded that there was no market for plaintiffs' gas to the pipeline companies (Opinion on Rehearing, R. 556).

(4) That absence of a market price is not established by proof of absence of daily sales on a fluctuating or competitive market (Opinion on Rehearing, R. 557).

(5) That a *prima facie* showing as to absence of market price was not made by showing that there was no market price in the county where the Bynum well was located, but that the burden was on plaintiffs to show that there was

no market price for gas in the "Panhandle Gas Field" (Original Opinion, R. 537), a field containing more than a million acres, extending 125 miles in length, and covering portions of 7 counties.

(6) That plaintiffs had failed to make a *prima facie* showing as to absence of market price at the well for the Bynum gas (Original Opinion, R. 537, and Opinion on Rehearing, R. 556).

(7) That certain evidence admitted was not admissible even to show the fair value of the gas (Original Opinion, R. 539, and Opinion on Rehearing, R. 556).

(8) That under Rule 49a of the Federal Rules of Civil Procedure the trial court should first require a special finding as to whether or not there existed a market price for the gas before receiving evidence on actual or reasonable value (Original Opinion, R. 540).

The Dissenting Opinion

In a vigorous dissenting opinion (R. 541) one member of the court expressed the conviction that the judgment of the trial court should be affirmed, insisting

(1) That plaintiffs had made a *prima facie* case, *and more,* both as to absence of market value, and as to the fair value of the gas, thus shifting to the defendant the burden "to go forward with the evidence" (R. 541).

(2) That since defendant, because of the lease contract, had all the facts in its possession, and knew accurately the "fair market value", the "fair value", and the "market price" of the gas, how much had been taken, when taken, where taken, and the actual cost of piping the gas to where it was delivered to defendant's plants and there used, and the residue thereof sold to others, it owed a duty to plain-

tiffs to disclose honestly the facts (R. 541); this under the principle recognized in *Selma, Rome & Dalton* vs. *U. S.*, 139 U. S. 560, 568; *Miller* vs. *Lykes Bros.-Ripley S. S. Co.*, (5th Circ.) 98 F. (2d) 185); and *Manufacturers' Finance Co.*, vs. *Marks*, (6th Circ.) 142 F. (2d) 521, 527, that "the burden of proof lies on the person who wishes to support his case by a particular fact which lies more peculiarly within his knowledge, or of which he is supposed to be cognizant."[3]

(3) That, when defendant refused to offer any evidence, resting its case, and thereby saying to the court, in effect, that

> "We know all this and more about the gas in question; we have taken over the one-eighth royalty gas, the proceeds from which belongs to the plaintiffs, and we have used it and sold it, but you find out, if you can, what became of it and its fair market value" (R. 541);

plaintiffs were entitled to a directed verdict (R. 542).

(4) That the opinions of the Court as to the evidence necessary to disclose fair market value of gas had been confusing and misleading; that lawyers and counsellors had not been able to use them as a guide and thereby escape reversal on appeal (R. 542), and that this case was being sent back for another long and difficult trial, with the issues, if possible, "more nearly cluttered up than they ever have been before" (R. 542).

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[3] This is also the rule applied in the state courts of Texas. *Barron* v. *Texas Employers' Insurance Association*, 36 S. W. (2d) 464, 467.

V

Reasons Relied on for the Allowance of the Writ

1. *The holding of the Court of Appeals that "in view of the Texas law that the royalty owner has no title even to the 1/8th part of the gas, and that only the contractual relation of creditor and debtor exists, we are unable to fasten the obligation to make a full disclosure where it really ought to be", is a decision on an important question of local law which is probably in conflict with applicable local decisions.*

The dissenting member of the Court insisted that, since Phillips under the lease had all the facts in its possession, and knew accurately the "fair market value", the "fair value", and the "market price", knew how much gas had been taken, when taken, where taken, and the actual cost of piping to the place of delivery, it owed a duty to plaintiffs to disclose honestly such facts; and it was the duty of the Court to call upon defendant to disclose fully, fairly and honestly those matters and facts which were peculiarly within its knowledge; that when defendant refused to offer any evidence as to matters which were peculiarly within its knowledge and which it gained by reason of the lease contract, plaintiffs were entitled to a judgment (R. 541-543).

The majority of the Court evidenced its desire so to hold, saying that it had searched for some principle of law that would permit it to announce that when lessee takes all the gas from a well and makes such a disposition of it as best suits its purpose under a contract which does not state a definite sum to be paid, there arose either a fiduciary relation or a relation as principal and agent which would place lessee under the duty to keep his principal fully informed and to disclose all facts that came to his knowledge and to fully and faithfully account to the lessor (R. 54).

Two members of the Court felt, however, that it was constrained to hold "in view of the Texas law that the royalty owner had no title even to the ⅛th part of the gas, and that only the contractual relation of debtor and creditor exists" that it could not "fasten the obligation to make a full disclosure *where it really ought to be*" (R. 540).

Thus, the entire membership of the Court recognized the well established rule that where there is a common interest in subject matter, and one of the parties has full charge and control of the subject matter and is in position to know all the facts with respect thereto while the other party is not in position to know such facts, the one having such control and having such knowledge must make a full disclosure, and little evidence is required on the part of the other to require him to go forward with the evidence; that the required quantum of evidence from one not in position to know all the facts with respect to the subject matter is not as great as in those cases where the parties are equally informed.[4]

While the Court recognized this to be the general rule, and evidenced a desire to apply it in this case, it felt that it was unable to do so because of the Texas law that the royalty owner has no "title" to the one-eighth part of the gas and only the contractual relation of creditor and debtor exists (R. 540). It cited *no* Texas case in support of its holding, and petitioners can only surmise as to what Texas doctrine is involved and what Texas cases the Court had in mind. It is, of course, the settled doctrine of the Texas

[4] See *Selma, Rome & Dalton R. R. Co.* v. *U. S.*, 139 U. S. 561, 568; *U. S.* v. *Denver & Rio Grande Ry. Co.*, 191 U. S. 84, 92; *Valdez* v. *Larringa*, 233 U. S. 705, 709; *Mammouth Oil Co.* v. *U. S.*, 275 U. S. 13, 52; *U. S. ex Bilokumsky* v. *Tod*, 263 U. S. 148, 153; *Interstate Circuit* v. *U. S.*, 306 U. S. 208, 226. This is also the principle applied in the state courts in Texas: *Ryan* v. *M. K. & T. Ry. Co.*, 65 Tex. 13, 19, 20; *Harper* v. *Highway Motor Freight Lines* (Dallas Ct. Civ. Ap.), 89 S. W. (2d) 448, 449; *Barron* v. *Texas Employers' Insurance Assn.* (Com. App.), 36 S. W. (2d) 464, 467.

courts that the owner of the fee owns full title to the gas in place, and by an oil and gas lease conveys that full title to lessee. No Texas court, however, has held, as an incident of that doctrine, that the lessee does not have the same obligation as that which would have existed if, as is true in most states, the fee owner had no interest in the gas in place.

The fiction of "ownership in place" with respect to oil and gas, and the theory that an oil and gas lease constitutes a conveyance of such oil and gas in place, were adopted by the Texas courts in order that *ad valorem* taxes on the value of such minerals and the estate granted by such oil and gas lease could be constitutionally sustained. *Stephens County* v. *Mid-Kansas O & G Co.*, 113 Tex. 160, 254 S. W. 290; *Hager* v. *Stakes*, 116 Tex. 453, 294 S. W. 835. If, as is usually the case as to royalty on oil, royalty is to be paid in kind, through a reservation, lessor continues to be the owner of that portion of the minerals in place (*Waggoner Estate* v. *Wichita County*, 273 U. S. 113, 118), while if he is to be paid a sum of money determined by the amount of production, full title to the gas in place passes to lessee.

No Texas court has held that, because of this Texas doctrine of ownership of minerals in place, and the theory that an oil and gas lease conveys a determinable fee title to the minerals in place, there is any difference between the obligations of a lessee under a lease in Texas and those of a lessee holding leases in other states which consider a lease to be only a license to explore, a profit a prendre, a corporeal hereditament, an incorporeal hereditament, a servitude, or as creating the relationship of landlord and tenant.

On the contrary, the Texas courts have consistently enforced an implied obligation, implicit in every lease without regard to the technical theory of the resulting relation, requiring diligence on the part of lessee in drill-

ing and producing wells and *marketing the production* therefrom in the mutual interest of *both* lessor and lessee. *Freeport Sulphur Co.* v. *American Sulphur Royalty Co.*, 117 Tex. 439, 6 S. W. (2d) 1039, 1042; *Petroleum Producers Co.* v. *Steffens*, 162 S. W. (2d) 698; *Waggoner Estate* v. *Sigler Oil Co.*, 118 Tex. 509, 19 S. W. (2d) 27, 29.

It is true that upon the production of gas there also arises a relationship of creditor and debtor binding lessee to pay lessor in accordance with the contract. That is true in all states, regardless of the theory of ownership obtaining. Nevertheless, it is clear that, in virtue of the sole control by lessee of both the production and the marketing of the gas, lessee is in much better position to know the facts as to available markets and market price than is lessor; and no Texas court has ever held that the Texas doctrine of ownership in place operates to relieve lessee of the obligation to render an accounting such as is required of a tenant to his landlord or under any other relationship where mutual interests in property or its disposition are involved, and such as exists in all other oil and gas producing states.

Certainly, little evidence should be required of a lessor to make a *prima facie* case. The Texas courts have followed the doctrine of this Court that where a negative is alleged and defendant is in possession of all the facts, while plaintiff is not, the failure of defendant to make a full disclosure of itself establishes a negative. See, for example, *Barron* v. *Texas Employers' Insurance Assn.*, (Comm. App.) 36 S. W. (2d) 464, 467 (issuance of insurance policy), where the court cited with approval the opinion of this court in *U. S.* v. *D. & R. G. Ry. Co.*, 191 U. S. 84, where, among other things, this Court said (p. 92):

> "When a negative is averred in pleading, or plaintiff's case depends upon the establishment of a nega-

> tive, and the means of proving the fact are equally within the control of each party, then the burden of proof is upon the party averring the negative; but when the opposite party must, from the nature of the case, himself be in possession of full and plenary proof to disprove the negative averment, and the other party is not in possession of such proof, then it is manifestly just and reasonable that the party which is in possession of the proof should be required to adduce it; or, upon his failure to do so, we must presume it does not exist, *which of itself establishes a negative.*"

It is obvious that in holding that because of the Texas law, it was unable to apply this well settled doctrine, the Honorable Circuit Court of Appeals has decided an important question of local law in a way probably in conflict with, and not supported by, applicable local decisions.

2. *The holding of the Court of Appeals that the phrase "market price at the well" in the Bynum lease does not mean "market price at the Bynum well," but means "the price which similar gas brings at the mouths of wells generally in the field" (R. 561), constitutes a decision of an important question of local law in a way probably in conflict with applicable local decisions.*

The Bynum well is located in Moore County, Texas. The Panhandle field covers portions of 7 counties, including Moore, and extends 125 miles in length, comprising 1,500,000 acres.[5] The Bynum well, producing sweet gas, is in approximately the center of Moore County (R. 242). 231 sweet gas wells in 1942 and 243 sweet gas wells in 1943 were located in Moore County (R. 475).

Plaintiffs interpreted the words "at the well" as fixing the point for determining whether or not a "market," as that term was used in the lease, existed from which

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[5] See *Thompson* v. *Consolidated Gas Utilities Corp.*, 300 U. S. 55, 59.

"market price" could be determined; and as authorizing, if there was no market price available at the well, a deduction of the cost of transportation, if its value, market or actual, at some other available point were shown. They showed that there was not, at the well, or at any other point in the county, a probable competitive purchaser for the gas from the Bynum well; that, in fact, there was not a single well in the county whose production was taken under circumstances which created or reflected the existence of a "market" or "market price"; and no facilities by which such gas could be transported, if a market were available elsewhere.

Plaintiffs' interpretation of the lease was rejected by the Court of Appeals. It held that the test was "whether or not there was a market price established by actual sales *in the Panhandle gas field*" (R. 537, 556); it assumed that the Bynum gas could be delivered to gasoline plants of other companies (R. 537) even though those companies had no pipelines in Moore County through which to transport the gas; assumed that other companies were purchasing gas of similar quality and availability (R. 537, 538) though their purchases in other counties which were shown were from wells of low pressure and low potentials, located at points approximately 100 miles from the Bynum well (R. 420-421, 236-241), and the production was taken under processing contracts rather than "market price" sales (R. 412). It held that proof by plaintiffs that there were no comparable sales in Moore County was not proof that there were *no* comparable sales by which "market price" could be shown (R. 557).

In thus rejecting plaintiffs' interpretation of the words "at the well" as fixing the "proper locus" for consideration in determining whether or not a "market price" existed,

the opinion of the Court of Appeals is in conflict with principles recognized and applied by the Texas courts:

(a) In *Danciger Oil & Refineries, Inc.*, v. *Hamill Drilling Co.*, (Tex. Sup. Ct.), 171 S. W. (2d) 321, 323, where the obligation was to pay "the prevailing market price paid by major companies in Gulf Coast Area," the court held that if there was no *market* in the *stipulated area*, then lessee was liable for the reasonable value of the gas produced. Petitioners here insist that the "stipulated area" provided for in the Bynum lease was "at the well."

(b) In *San Antonio & Arkansas Pass. Ry. Co.* v. *Liggett*, (3 Ct. Civ. App.) 252 S. W. 191, it was held that the owner could prove the intrinsic value of an automobile in Falls County, even though there was a market for the car at Waco, in an adjoining county.

(c) In *Ara* v. *Rutland* (Comm. App.), 215 S. W. 445, it was held that a necessary element in showing market value "is to show by the testimony that this market value is that at *the place designated* by the law as furnishing *the proper locus of the market* from which the value is to be determined."

The novel holding of the Court in this case that "market price at the well" does not fix the point at which the existence *vel non* of a market shall be determined is not only in conflict with the principles of the Texas cases referred to; it is also in direct conflict with holdings in other gas producing states, and former opinions of the *same* Circuit Court of Appeals.

That holding is that the term "market price at the well" does not mean market price at the Bynum well; but it means "the price which similar gas brings at the mouths of wells generally in the field." Thus, it makes determina-

tive of the value of the Bynum gas, the prices which similar gas brings at the mouths of wells generally in the field, without regard to whether the Bynum gas is available to the same outlet as other gas, whether the prices paid for other gas are paid on a competitive market, whether the prices paid for such other gas are based on long time contracts, and regardless of what Phillips itself obtains for the gas.

The expression "market price at the well" is a common expression in general use in the drafting of oil and gas leases in all the oil producing states. Until now it has always been interpreted as fixing the *point* at which value shall be determined and, if the gas is marketed elsewhere, authorizing lessee to make a deduction of such expense as is incurred in transporting the gas to the point of marketing or to the point of utilization.

Thus, in *Clear Creek Oil & Gas Co.* v. *Bushmiaer* (Ark.), 264 S. W. 830, 832, the lease provided for one-eighth royalty, and that "the market price of royalty gas at the well" should be the basis for payment. Lessee was, at a cost of 3½¢ per MCF piping the gas to points several miles distant where the gas was sold at 10¢ per MCF. It sought to pay its lessors 2½¢ as the "market price," since that was the price being paid by other companies to owners of gas wells *in the same field*. The court rejected that contention and held that the "market price" under those circumstances was the price received at the distant points less cost of transportation.

In that case, the court held that since there was *no market value* at the point of delivery, the *value* could be determined by ascertaining the value at the nearest place where the product *could be sold*, and deducting the cost of transportation; that this would show the *value* of the product as nearly as it was possible to show such value.

The Louisiana leases involved in *Sartor* v. *United Gas Public Service Co.* (5 Circ.) 84 F. (2d) 436, provided for calculating royalty at the "rate of market price at the well." The court held that there should be determined, first, *the daily market price at the well,* or at the *nearest market,* less costs of getting it there; and, second, if there was no daily market price, what the gas was actually worth; that plaintiffs should have, and defendant should pay them for, the market value at the well if there was one, the actual value *there* if there was not (p. 440).[6]

The rule that value, when no market price exists at the point selected, can be established by showing the market value at some other point less the cost of transportation to that point cannot be applied here because there is (a) no evidence of a market price at any other point, and (b) no transportation facilities are available by which the Bynum gas could be transported to such other point. Therefore, some other means for determining value must be used.

In view of the holdings of the Texas cases that market price is to be determined at the point where liability is incurred, it must be assumed that the Texas courts would permit the showing of fair value if there was, in fact, no market or market price in the vicinity of the well, and that a showing as to the situation in the entire county was *prima facie* sufficient. The interpretation of the lease made by the Court of Appeals is obviously not in harmony with the principles of the Texas cases, and those from other gas producing states.

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[6] See also *Hemler* v. *Hope Producing Co.* (5th Circ.), 117 F. (2d) 231, 232; *Union Producing Co.* v. *Pardue,* 117 F. (2d) 225; *Hemler* v. *Union Producing Co.,* 134 F. (2d) 436, 438; *Sartor* v. *Arkansas Natural Gas Co.,* 321 U. S. 620, 622.

3. *The holding of the Circuit Court of Appeals that, although showing there is no market or market price for gas either at the Bynum well or at any other well in Moore County, plaintiffs were not entitled to show the fair value of the gas is of such tremendous importance to the land and royalty owners in the Panhandle gas field (the largest in the world) that the question involved is of such gravity as justifies its consideration and determination by this Court.*

This Court knows from the record in *Thompson* v. *Consolidated Gas Utilities Corporation,* 300 U. S. 55, that the Texas Panhandle gas field is one of tremendous size, extending through seven counties for a distance of 125 miles in length, having a width ranging from 10 to 40 miles, and producing both sweet and sour gas; that for administrative purposes the field has been divided into the East field and the West field; that the sweet gas area of the East field embraces 181,000 acres and the sweet gas area of the West field 723,000 acres, a total of 904,000 acres; that as early as 1935 there were 517 wells producing sweet gas in the West field (in which Moore County is located) and 322 wells in the sweet gas area of the East field.

This Court also judicially knows that it is the practice in the gas fields for wells to be drilled under leases executed by the farmers and other owners of land in the area, in which leases provision is made for the retention by the land owner of a royalty (usually one-eighth) interest in the production; that sometimes this royalty is measured by the "proceeds" of the gas, and sometimes by the "market price at the well;" and that usually the leases are prepared by the lessee.

It can, therefore, be readily recognized that whether a royalty owner under one well cannot make a prima facie showing of absence of market price at the well by showing the absence of such market or market price at his well,

or at any other place in the vicinity of his well (the entire county, for example) is of tremendous importance to many royalty owners.

If the holding of the Court of Appeals is sound, the result is, of course, of no consequence. The result, however, is of importance in determining whether or not the court has unduly shackled the land and royalty owner in his efforts to obtain for his royalty gas the compensation contemplated by his lease.

In this connection, it is suggested that in this case the court has made a fetish of the words "market price." If the courts are to reject the ordinary meaning of that term as being the price paid on a competitive market either at the point named in the contract, or at some other convenient point to which the gas can be transported by existing transportation facilities (with allowance for cost of transportation), consideration should be given to determining whether the term "market price" is not, in fact, an inept expression and used in the sense of "fair price" or "fair value."

4. *The holding of the Court of Appeals that prices paid their royalty owners under similar or comparable royalty provisions by pipeline companies owning gas wells in Moore County, and prices paid by such companies to other producers of gas under long term contracts, either at the well or delivered into their pipelines, were not admissible in evidence for consideration by the jury in reaching a determination as to the fair value of plaintiffs' royalty gas is the decision of an important question of local law probably in conflict with applicable local decisions.*

After, as they thought, making a prima facie showing as to the absence of a market price at the well for their royalty gas, plaintiffs showed the prices paid by the several pipeline companies to their royalty owners under similar

royalty provisions. The prices so paid ranged from 4¢ to 8¢ per MCF. They also showed prices being paid by one of those pipeline companies under long term contracts to other producers. In some instances the gas so purchased was taken at the well, and in others, delivery was made to the pipeline. Most of these sales were at 3½¢ (R. 72, 272). They also showed that after extracting the gasoline content Shamrock was selling its residue gas to a smelter in the county at 4.02¢ (R. 403).

These prices were shown, not as market prices, or even as measuring fair value, but only for consideration by the jury in reaching a determination of the fair value.

In presenting this evidence, counsel felt that they were following former rulings of that same court of appeals.

Thus, it was felt that evidence as to royalties being paid under leases in the county substantially similar to plaintiffs' lease was admissible under the holding in *Arkansas Natural Gas Co.* v. *Sartor*, 78 F. (2d) 924, 926, that "the stipulation as to average prices paid under contracts substantially similar to the lease in suit was *improperly excluded*".

They felt that it was appropriate to show on the issue of fair value the prices being paid for royalty gas in the county under leases and division orders fixing stipulated prices in view of the same court's holding in *Sartor* v. *United Gas Public Service Co.*, 84 F. (2d) 436, 439, followed in *Hemler* v. *Hope Producing Co.*, 117 F. (2d) 231, 232, and *Sartor* v. *Arkansas Natural Gas Corporation*, 134 F. (2d) 433, that included among the factors properly bearing upon the establishment of fair value is "the fixed royalties obtaining in the leases in the field in the light of their respective dates".[7]

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[7] See the approval of that substantive rule in this Court's reference to that holding in its opinion in the last cited case—*Sartor* v. *Arkansas Nat. Gas Corp.*, 321 U. S. 620, 622.

They also felt that evidence as to prices paid by pipeline companies to other producers in the field, though sales were small in number, and the company purchasing was making no new connections, was appropriate for consideration in a determination of fair value in view of the same court's express holding in *Sartor* v. *United Public Service Co.*, 84 F. (2d) 436, 441, followed in subsequent cases, that on that issue "prices paid under the pipeline contracts" were admissible.

With respect to all such prices, the court charged the jury that factors of remoteness or difference of circumstances attending the prices considered must be given appropriate consideration (R. 500).

It was not contended that these prices constituted the only factors or circumstances appropriate for consideration in determining fair value. Obviously, one of the *best* evidences of that value would have been what Phillips did with the gas and what it realized out of the gas. It is reasonable to assume, since it failed to make a showing on that point, that it obtained more than those prices.

The admissibility of this evidence is clearly supported by the Texas cases. Their holdings are summarized in 17 *Tex. Juris.*, p. 438, sec. 162, in the following language:

> "The intrinsic value of property must be ascertained from the circumstances of the case, and a wide latitude in the evidence is permissible to enable the jury intelligently to determine such value. In general, *any* facts may be shown which would naturally affect the minds of the parties buying and selling in determining the price to be asked or given • • •"

What would be thought by a prospective buyer or purchaser more representative of fair value than the prices being paid and received by others, even though the person buying was making no additional purchases?

The Court of Appeals held that the prices paid their royalty owners by pipeline companies were influenced by the assumed fact that since those companies are subject to rate regulation, the prices they pay their royalty owners for their ⅛th royalty will probably be reflected in the compensation such companies receive for the ⅞ths which they own (R. 540). The companies referred to in that statement are Texoma Natural Gas Company (a part of the system of Natural Gas Pipeline Company of America), Panhandle Eastern Pipe Line Company, and Canadian River Gas Company. This Court judicially knows that as to those companies the Federal Power Commission has never adopted that theory of rate making, but has consistently followed the theory of a fair return on a determined rate base.[8]

5. *As a result of the Court's opinion in this case, the decisions of the Fifth Circuit Court of Appeals with respect to the substantive rights of a lessor under an oil and gas lease providing for payment of royalty at the market price at the well, and the evidence appropriate for consideration in a suit involving those rights, are in such a chaotic and confused state as calls for the exercise by this Court of its supervisory powers by granting a writ of certiorari and thereafter the issuance by this Court of an authoritative and elucidating decision with respect to such matters.*

Texas and Louisiana, two of the largest gas producing states, are both included in the jurisdiction of the Court of Appeals for the Fifth Circuit. It is obvious, therefore, that decisions of that court interpreting the provisions of an oil and gas lease, and the character of evidence

[8] See *Federal Power Commission* v. *Natural Gas Pipeline Company of America*, 315 U. S. 575; *Canadian River Gas Co.* v. *Federal Power Commission*, 65 Sup. Ct. 829; *Panhandle Eastern Pipe Line Co.* v. *Federal Power Commission*, 65 Sup. Ct. 821.

appropriate for consideration in litigation with respect to the rights of the parties under such leases are of tremendous importance, not only to the bench and bar, but also to every operator and every royalty owner. If the decisions of that court are in irreconcilable conflict, so that counsel and trial judges cannot with safety rely on any, the situation is one that calls for an exercise by this Court of its power of supervision, even more than would be the case if the conflicting decisions were from different circuits.

In the dissenting opinion in this case, it was pointed out that former opinions of the Court seemed to have been confusing and misleading; that lawyers and counselors had not been able to use them as a guide and thereby escape reversal when coming to that court on appeal (R. 542).[9] It was also said in that dissenting opinion that

> "This case * * * must now go back for another long and difficult trial, *with the issues, if possible,* I submit, *more nearly cluttered up than they have ever been before.*[9a] After paying all costs, the plaintiff must again try to prove the 'market price' of the gas 'at the mouth of the well', *when as a matter of fact there is no such market price,* and failing in this, then go to the defendant and beg it to kindly inform as to the fair market value of one-eighth royalty gas it has taken over, the net proceeds of which belong to plaintiff" (R. 542).

A review of former opinions shows that the decisions of the Fifth Circuit are now in hopeless confusion as to the rights of a royalty owner under a lease providing for payment of "market price at the well," when he may show "fair value," and the character of evidence admissible on

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[9] Observing that one case, *Arkansas Natural Gas Co.* v. *Sartor,* had been before that court at least *six times,* and was finally affirmed on January 23, 1946.

[9a] All emphasis in this motion by italics is supplied.

the issue of fair value. As briefly as possible, the holdings of that court are reviewed.

In *Arkansas Natural Gas Co.* v. *Sartor,* 78 F. (2d) 924 (Judges Bryan, Foster and Sibley sitting; Opinion written by Judge Foster of *Louisiana*), it was held that the term "market *price*" was interchangeable with the term "market *value*"; that in the nature of things there could be no open *market* for natural gas since there were no quotations or other evidence to be obtained of "open and notorious market prices at which any one desiring gas could purchase it"; that *value* might be shown by evidence of other sales, if conditions were substantially similar; that other sales might be shown by verbal testimony or by documentary evidence (p. 927), but that certain contracts providing for pipeline deliveries were not admissible because of guaranties of large deliveries of gas contained therein; and that evidence as to prices paid under contracts substantially similar to the lease in suit was *improperly excluded* (p. 928).[10]

Next came *Sartor* v. *United Gas Public Service Co.,* 84 F. (2d) 436 (Judges Foster, Hutcheson and Holmes sitting; Opinion by Judge Hutcheson of *Texas*). The court there held that while the pipeline delivery contracts themselves were not admissible, it was permissible to show the prices paid thereunder on the issue of *fair value* (p. 439); that the purpose of the inquiry should be to determine (1) if it can be done, the *daily market price at the well,* or at the nearest *market,* less costs of getting it there, and (2) if there was no *daily* market price, to determine what the gas is actually worth *at the well;* that plaintiffs should have, and defendant should pay them for, one-eighth of the gas taken, the market value *at the well*

[10] In this case the court has held that such evidence was improperly *admitted.*

if there was one, the actual value *there* if there was not (p. 440); that in determining this *fair value,* every factor properly bearing upon its establishment should be taken into consideration, including *fixed royalties* obtaining in leases in the field and prices paid under pipeline contracts (pp. 440-441).[11]

Then the group of cases, decided June 16, 1941—*Union Producing Co.* v. *Pardue,* 117 F. (2d) 225; *Union Producing Co.* v. *Driskell,* 117 F. (2d) 229; and *Hemler* v. *Hope Producing Co.,* 117 (2d) F. 231. Judges Sibley, Hutcheson and McCord sat in all three cases, with Judges Sibley, Holmes and McCord sitting in the *Hemler* case on hearing.

In the *Pardue* and *Driskell* cases the court rejected the contention of the company that prices paid by the pipeline companies were inadmissible (p. 227), and in the *Hemler* case rejected the contention of the royalty owner that prices set forth in lease contracts in the field were inadmissible (p. 232).

In the *Pardue* case, it was observed that since plaintiffs' leases contemplated that he should have the benefit of day by day advances in the market, it was obvious that in a field controlled and dominated by a few producing and pipeline companies, evidence of a few sales at the well on a few of those days and evidence of lease contracts fixing a price for the term of the leases was not such evidence of *day by day market value at the well* as would exclude resort to other considerations fully canvassed in former opinions (p. 227).[12]

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[11] In this case, the court has held such evidence inadmissible either on the issue of market value or on the issue of fair value (R. 556).

[12] Obviously referring to 78 F. (2d) 929 and 84 F. (2d) 486.

In the *Hemler* case, it said that the case was tried faithfully by the rules theretofore laid down and that

> "To reverse the judgment in it would be • • • to reverse court and counsel for pursuing the course we have laid down, following the track we have marked out in former opinions" (p. 232).

Finally, as to the Louisiana cases, in *Hemler* v. *Union Producing Company,* 134 F. (2d) 436 (Judges Hutcheson, Holmes and McCord sitting), it was contended by the company that the evidence conclusively established the existence of a market *at the well* in such conclusive form as to prevent resort to pipeline prices or other method of showing *value* at the well. The court said, however, that while the evidence did show such market value during a portion of the period, yet it was insufficient to establish as a matter of law that there was a "day by day, week by week, or month by month market price of 3 cents or less at the well"; but that within the rule "laboriously spelled out" in former cases the record presented "genuine issues of fact as to whether there was a *day by day* market price as to any or all of the period in question, and if as to any part or all of it there was not such market price, what was the *value* at the well" (p. 438).

It is at once obvious that the holdings in the present case with respect to the admissibility of evidence as to prices paid by pipeline companies to other producers, and the fixed royalty prices obtaining in other leases, as hearing on the question of fair value, cannot be in harmony with former holdings of the court.

Nor, if true, does the circumstance referred to in the opinion on rehearing (R. 556) that in the Richland gas field the gas was readily marketable to pipeline companies whereas in the Panhandle field only a portion of the gas produced is taken by pipelines constitute any valid ground

of distinguishment in law. As a matter of fact, a portion of plaintiffs' gas was disposed of by Phillips (amount undisclosed) to Texoma Natural Gas Company, a portion to Cactus Ordnance Works (amount undisclosed), and a portion (amount undisclosed) utilized in Phillips' own operations (R. 438).

While, in his opening statement, counsel for Phillips promised to show that, after extracting the gasoline content from the gas, it sold the residue for the best price obtainable (R. 61-63), it *never did make that showing.* Although saying a portion was sold for 1¢, some for 3¢ and some for 5¢, it made no showing as to how much it sold for either price.

Under such circumstances it is clear that the rules of the various Louisiana cases should be applied, and that the evidence presented by plaintiffs was admissible for consideration by the jury.

Nor are the Texas cases, *Shamrock O&G Co.* v. *Coffee,* 140 F. (2d) 409; *Ochsner* v. *Phillips Petroleum Co.,* 146 F. (2d) 138; and *Record* v. *Phillips Petroleum Co.,* 146 F. (2d) 485, in conflict with the Louisiana cases. In each of those cases, counsel for plaintiffs sued for *market value, conceded that a market price existed,* and that approximately that price had been tendered. In one case it was contended that the admitted market price was collusive, and in the others that the character of use of particular gas was different from that in the conceded general market.

In this case, however, there was no concession as to the existence of a "market" or "market price" for *any* use; nor did any witness in this case, as did numerous witnesses in those cases, testify as to such market price or market. Plaintiffs' counsel, therefore, had no opportunity to cross-examine any of the witnesses on whose testimony the court

assumed the existence of a market in the *Coffee, Ochsner* and *Record* cases.

It is respectfully submitted that the holdings of the Fifth Circuit Court of Appeals are such that the trial court cannot know on another trial what the law actually is; and, in the interest of the royalty owners in Texas and Louisiana, an authoritative holding should be made as to what constitutes a "market price at the well," and what evidence is admissible on the issue of fair value, whether the well be in the small Richland field in Louisiana (seven by ten miles, and containing 50,000 acres) or in the enormous Panhandle field (125 miles in length, from 10 to 30 miles in width, and containing 1,500,000 acres).

Conclusion

It is therefore respectfully submitted that this case is one calling for the exercise by this Court of its supervisory powers in order that justice may be done, and that to such an end a writ of certiorari should be granted and this Court should review the decision of the United States Circuit Court of Appeals for the Fifth Circuit and finally reverse it.

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